

Message Text

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AMEMBASSY BELGRADE

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SUBJ: ECONADS: REPORT ON RECENT TRENDS IN YUGOSLAV ECONOMY

REF: A. USNATO 387 B. USNATO 416 C. USNATO 590

1. DURING JANUARY 23 ECONOMIC COMMITTEE MEETING TO EXCHANGE VIEWS ON DRAFT REPORT ON YUGOSLAV ECONOMY (AC/127-WP/413 AND CORRIGENDUM), CANADIAN ECONAD DISTRIBUTED PRELIMINARY COMMENTS FROM CANADIAN EMBASSY BELGRADE (REF A). IN PREPARATION FOR FEB 13 MEETING, CANADIAN DELEGATION HAS NOW CIRCULATED MORE DEFINITIVE APPRAISAL FROM OTTAWA (PARA 2 BELOW). SINCE REPORT ON YUGOSLAV ECONOMY HAS BEEN ON ECONAD AGENDA FOR ONE MONTH, MISSION WOULD APPRECIATE WASHINGTON COMMENTS PRIOR TO FEBRUARY 13 MEETING.

2. BEGIN TEXT.

TO PREPARE FOR THE NEW YEAR, YUGOSLAVIA'S FEDERAL ASSEMBLY ROUNDED OUT THE OLD BY ADOPTING A RESOLUTION ON ECONOMIC AND SOCIAL DEVELOPMENT FOR 1975. THIS RESOLUTION CONTAINS THE OBJECTIVES OF YUGOSLAVIA'S ECONOMIC POLICY IN
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1975. EXPECTED SHORTLY IS A LONG-TERM DEVELOPMENT PLAN FOR THE PERIOD TO 1985.

2. STATISTICALLY, MANY YUGOSLAV INTERNAL ECONOMIC INDICES SHOWED A FAVORABLE GROWTH FROM 1973 LEVELS, INCLUDING

(WITH COMPARABLE 1973 RATES IN BRACKETS); GROSS NATIONAL PRODUCT- UP 7PCT (5PCT); IN DUSTRIAL PRODUCTION- UP 9-10 PCT (6PCT); EMPLOYMENT- UP 5PCT (2PCT); AND PRODUCTIVITY- UP 5PCT (2.5). TOURIST EARNINGS INCREASED 11PCT IN 1974. AGRICULTURAL PRODUCTION ALSO ROSE 3PCT, INCLUDING A RECORD WHEAT HARVEST (6.3 MILLION TONS) UP 32PCT OVER 1973. NOMINAL PERSONAL INCOMES ROSE 28PCT (16PCT) FOR AN ESTIMATED OFFICIAL RISE IN REAL INCOME OF ABOUT 6PCT, AS COMPARED WITH A DECLINE OF 3PCT IN 1973. AS ELSEWHERE, STRONG INFLATION CONTINUED IN YUGOSLAVIA. THE OFFICIAL COST OF LIVING ROSE 21PCT AS COMPARED WITH 20PCT IN 1973 WHILE RETAIL AND WHOLESALE PRICE INDICES GREW AT A SOMEWHAT FASTER RATE.

3. IN EXTERNAL TRADE, 1974 WAS A DIFFICULT YEAR FOR THE YUGOSLAV ECONOMY. AFTER 2 SUCCESSIVE BALANCE OF PAYMENTS SURPLUSES, YUGOSLAVIA HAS A DEFICIT FOR 1974 OF AT LEAST \$720 MILLION. THIS DERIVES DIRECTLY FROM A TRADE DEFICIT OF AROUND \$3.7 BILLION WHICH WILL NOT BE COMPLETELY OFFSET BY THE TOURIST EARNINGS AND REMITTANCES FROM GUESTWORKERS ABROAD WHICH ARE FUNDAMENTAL FACTORS IN YUGOSLAVIA'S PAYMENTS SITUATION. OFFICIAL FIGURES PUT THE YEAR'S INCREASE IN VALUE OF YUGOSLAV EXPORTS AT 33PCT AGAINST AN INCREASE IN IMPORTS OF 67PCT. IN REAL TERM, THE INCREASE IN EXPORTS WAS ONLY 3PCT AGAINST

AVERAGE PERSONAL INCOME FOR SEPT 1974 HAS BEEN REPORTED AS 2504 ND/MONTH (APPROX \$145 CDN) IN A RANGE OF 2000-3800 ND MONTHLY (\$115-210 APPROX).

A REAL RISE OF ABOUT 14PCT IN IMPORTS COMPARED WITH PLANNED GROWTH OF 9-10PCT AND 12PCT RESPECTIVELY. IN ADDITION, WHILE EXPORT PRICES ROSE 32PCT, IMPORT PRICES GREW ABOUT 47PCT (AND ABOUT 68PCT FOR BASIC MATERIALS). EARNINGS FROM EXPORTS THEREFORE COVERED ONLY ABOUT 50PCT OF THE COST OF YUGOSLAVIA'S IMPORTS. ONE MAJOR FACTOR WHICH HURT YUGOSLAVIA'S EXPORT PERFORMANCE IN 1974 WAS THE LIMITED OFFICIAL USE
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EEC'S BAN ON BEEF IMPORTS WHICH STRUCK HARD AT A MAJOR YUGOSLAV EXPORT. THE TRADE DEFICIT WAS AGGRAVATED BY THE STRUCTURE OF YUGOSLAV IMPORTS, ABOUT 2/3 OF WHICH ARE CRUDE OIL, FOODSTUFFS AND RAW MATERIALS, SECTORS WHERE PRICE RISES HAVE BEEN GREATEST. PURCHASE OF NON-ESSENTIAL CONSUMABLES AND OVER-INVESTMENT IN INVENTORIES (A HEDGE AGAINST INFLATION) AND FOREIGN EQUIPMENT ARE ALSO BEING PARTIALLY BLAMED FOR THE TRADE DEFICIT.

4. DESPITE THE TRADE DEFICIT, YUGOSLAV SOURCES REPORT THAT 18-20PCT OF YUGOSLAVIA'S ANNUAL FOREIGN EXCHANGE EARNINGS ARE SUFFICIENT TO MEET ITS ANNUAL EXTERNAL DEBT REPAYMENT

OBLIGATIONS. THIS 20PCT RATION IS RETAINED AS A CEILING FIGURE IN THE RESOLUTION ON ECONOMIC AND SOCIAL POLICY FOR 1975.

A RECENT DOCUMENT OF THE IBRD DATED NOVEMBER 11, 1974 (REPORT NO. P-1498A -YU) CONCLUDES (P.5) THAT "YUGOSLAVIA REMAINS CREDIT-WORTHY FOR A SUBSTANTIAL AMOUNT OF BANK LENDING".

5. WHILE OVERALL, YUGOSLAVIA'S FOREIGN TRADE TURNOVER (EXPORTS PLUS IMPORTS) GREW 54PCT IN CURRENT VALUE IN 1974, THE STRONGEST GROWTH WAS IN TRADE WITH THE DEVELOPING COUNTRIES, AN INCREASE OF 93PCT AGAINST INCREASES WITH THE SOCIALIST AND DEVELOPED COUNTRIES OF 61PCT AND 43PCT RESPECTIVELY. # ALTHOUGH YUGOSLAVIA'S OVERALL TRADE WITH THE DEVELOPED COUNTRIES GREW AT A SLOWER RATE IN 1974 THAN WITH EITHER THE DEVELOPING OR SOCIALIST COUNTRIES, THE OVERALL GEOGRAPHIC DISTRIBUTION OF YUGOSLAVIA'S EXTERNAL TRADE DID NOT SHIFT SIGNIFICANTLY. THE DISTRIBUTION WITH COMPARATIVE 1973 FIGURES IN BRACKETS WAS: 56PCT (60PCT) WITH THE DEVELOPED COUNTRIES; 29PCT (28PCT) WITH THE SOCIALIST COUNTRIES; AND 14PCT (11PCT) WITH THE DEVELOPING STATES. ## OVERALL, YUGOSLAVIA'S TRADE, PARTICULARLY IMPORTS, REMAINED HEAVILY LINKED TO THE DEVELOPED WEST. EFFORTS TO INCREASE EXCHANGES WITH THE DEVELOPING COUNTRIES HAVE BORN SOME FRUIT, PARTICULARLY IN IMPORTS, AND GREAT STRESS CONTINUES TO BE PLACED HERE ON EFFORTS TO EXPAND TRADE WITH THESE COUNTRIES IN KEEPING WITH YUGOSLAVIA'S STRONG ADHERENCE TO NON-ALIGNMENT AND JOINT ECONOMIC EFFORTS BY DEVELOPING STATES. IN TERMS OF CONVERTIBILITY, LIMITED OFFICIAL USE LIMITED OFFICIAL USE

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72PCT (71PCT) OF YUGOSLAVIA'S TRADE WAS IN CONVERTIBLE CURRENCY, 26PCT (25PCT) IN EAST EUROPEAN CLEARING ACCOUNTS AND 1PCT (3PCT) IN OTHER CLEARING ARRANGEMENTS. THE CONVERTIBLE PORTION SHOULD INCREASE SOMEWHAT THIS YEAR SINCE, WITH RECENT AGREEMENTS,

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BROKEN DOWN, YUGOSLAVIA'S EXPORTS TO THE DEVELOPING STATES GREW 54PCT WHILE IMPORTS INCREASED 113PCT. EXPORTS TO THE SOCIALIST COUNTRIES GREW 64PCT IN 1974 AND IMPORTS 59PCT WHILE THE CORRESPONDING FIGURES FOR THE DEVELOPED COUNTRIES WERE 11PCT AND 62PCT RESPECTIVELY.

BROKEN DOWN INTO EXPORTS AND IMPORTS THE GEOGRAPHIC DISTRIBUTION OF YUGOSLAVIA'S TRADE WAS:

	EXPORTS		IMPORTS		
	1974	1973	1974	1973	
DEVELOPED	46PCT	56PCT	60PCT	62PCT	
SOCIALIST	41PCT	34PCT	24PCT	24PCT	
DEVELOPING	11PCT	9PCT	15PCT	12PCT	NOTE...

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IN EXPORTS THERE WAS A SHIFT OF 10PCT AWAY FROM DEPENDENCE ON WESTERN MARKETS IN FAVOUR OF THE SOCIALIST (7PCT) AND DEVELOPING (2PCT) COUNTRIES. IN IMPORTS, DEVELOPING SOURCES LIMITED OFFICIAL USE
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GAINED SLIGHTLY (3PCT) AT THE EXPENSE OF WESTERN SUPPLIERS. EFFORTS TO INCREASE EXPORTS AND DECREASE IMPORTS IN 1975 TO OVERCOME 1974'S TRADE DEFICIT COULD REDUCE SOMEWHAT FURTHER YUGOSLAVIA'S DEPENDENCE ON TRADE WITH THE DEVELOPED COUNTRIES.

YUGOSLAVIA NOW HAS UNDERTAKINGS TO SETTLE TRADE BALANCES IN CONVERTIBLE CURRENCY WITH ROMANIA, HUNGARY, POLAND AND BULGARIA (ALSO CHINA AND KOREA). THE USSR, CZECHOSLOVAKIA AND THE GDR ARE HOWEVER YUGOSLAVIA'S LEADING COMECON PARTNERS. INCOMPLETE FIGURES FOR 1974 INDICATE THAT THE BIG THREE YUGOSLAV TRADE PARTNERS IN ORDER ARE THE FEDERAL REPUBLIC OF GERMANY (FRG), THE USSR AND ITALY.

6. THE MAJOR ECONOMIC PROBLEMS WHICH THE RESOLUTION FOR 1975 IS DESIGNED TO COMBAT ARE INFLATION, THE BALANCE OF PAYMENTS (TRADE DEFICIT) PROBLEM, AND OVER-EXPENDITURE OF OVER-INVESTMENT IN NON-PRODUCTIVE GOODS. THE RESOLUTION LAYS BROAD STRESS ON SAVING IN 1975 AND ON EFFORTS TO REDUCE THIS YEAR'S TRADE DEFICIT. THE RESOLUTION AIMS AT AN INCREASE IN REAL INCOME WHICH IS LESS THAN THE GROWTH OF PRODUCTIVITY (TARGETTED AT 3.5PCT) TO ENCOURAGE PRODUCTIVE RE-INVESTMENT AND SAVING. INVESTMENT IN CAPITAL EQUIPMENT IS EXPECTED TO RISE 9.5PCT AND, OF COURSE, TO AID IN INCREASING FUTURE PRODUCTIVITY AND EXPORT PERFORMANCE.

TO CONTROL SPENDING, AS AN ANTI-INFLATIONARY MEASURE, AND INTER-REPUBLICAN AGREEMENT HAS BEEN CONCLUDED AS AN IMMEDIATE FOLLOW-UP TO THE 1975 RESOLUTION, TO LIMIT THE GROWTH OF GENERAL GOVERNMENT EXPENDITURE AT THE REPUBLICAN AND REGIONAL (COMMUNAL) LEVELS TO ABOUT 3/4 THE NOMINAL RATE OF GROWTH OF THE NATIONAL PRODUCT. THUS, FOR EXAMPLE, THE GROWTH IN SPENDING IN BOSNIA-HERCEGOVINA IS PLANNED TO BE HELD TO ABOUT 2/3 THE NOMINAL RATE OF GROWTH OF THE NATIONAL PRODUCT AND TO ABOUT 4/5 THAT RATE IN MONTENEGRO, CROATIA, MACEDONIA AND VOJVODINA AND SLIGHTLY LESS IN SERBIA. UNDER THE FEDERAL BUDGET RECENTLY ADOPTED GOVERNMENT SPENDING WILL INCREASE BY 23PCT WHICH APPARENTLY RESPECTS THE GENERAL TARGET ON SPENDING INCREASES MENTIONED ABOVE. THE FEDERAL BUDGET TOTALS 58,165 MILLION ND (CURRENTLY 17.34 ND

\$1 CDN) TO BE FINANCED 28,191 MILLION ND FROM FEDERAL SOURCES, 26,474 MILLION ND FROM CONTRIBUTIONS BY THE REPUBLICS AND PROVINCES AND 3,500 MILLION ND IN FEDERAL BOND ISSUES. IN A FURTHER EFFORT TO LIMIT DOMESTIC CONSUMPTION AS AN ANTI-INFLATIONARY LIMITED OFFICIAL USE
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TOOL, SLOVENIA HAS ACCEPTED A GOAL OF ONLY 1PCT GROWTH IN REAL PERSONAL INCOME FOR 1975 AND THE OTHER REPUBLICS 2.5-5PCT.

7. IN FOREIGN TRADE, THE TARGET IS TO INCREASE EXPORTS BY A REAL 10PCT WHILE HOLDING IMPORTS TO A REAL GROWTH OF ONLY 4PCT. THIS WILL REQUIRE CURTAILING MANY NON-ESSENTIAL IMPORTS. THE RESOLUTION CALLS FOR EFFORTS TO SAVE ON CRUDE OIL CONSUMPTION SINCE THE INCREASED COST OF CRUDE OIL ALONE WILL ACCOUNT FOR A DETERIORATION IN THE 1974 BALANCE OF TRADE ON THE ORDER OF ABOUT \$600 MILLION. THE 1974 HARVEST RESULTS ARE EXPECTED TO REDUCE IMPORT REQUIREMENTS OF SOME EDIBLES IN 1975. BESIDES THE RECORD WHEAT HARVEST, THE SUGAR BEET CROP IS ALSO UP 27PCT OVER 1973. DESPITE HEAVY FALL FLOODING, THE CORN HARVEST REACHED 97PCT OF THE 1973 CROP; ON THE OTHER HAND, THE SUNFLOWER HARVEST FOR EDIBLE OILS IS DOWN ABOUT 30PCT. MATERIAL STOCKS FOR PRODUCTION ARE ALSO SAID TO HAVE BEEN BUILT UP IN 1974 THIS REDUCING PURCHASE REQUIREMENTS IN 1975. THE OVERALL TARGET IN FOREIGN TRADE IS TO INCREASE THE PROPORTION OF IMPORTS COVERED BY EXPORTS FROM 1974'S 50PCT TO SOMETHING APPROACHING 70PCT. IN THE LONGER TERM, THE INTENTION IS TO GIVE PRIORITY IN DEVELOPMENT PLANS TO ENERGY, FOOD AND RAW AND BASIC MATERIAL RESOURCES TO CORRECT THE STRUCTURAL IMPORT PROBLEM (ABOUT 2/3 OF IMPORTS BEING FROM THESE SECTORS) WHICH YUGOSLAVIA CURRENTLY HAS.

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8. BESIDES THE FOREIGN TRADE TARGETS OUTLINED ABOVE, THE RESOLUTION ALSO SETS A 6PCT TARGET FOR GROWTH IN THE NATIONAL PRODUCT, 1PCT LESS THAN 1974'S ESTIMATED GROWTH, AND A 7-7.5PCT TARGET FOR INDUSTRIAL GROWTH, LESS BY 2-3PCT THAN THE ESTIMATED 1974 PERFORMANCE.

9. THE RESOLUTION ALSO AIMS AT A CONTINUING GROWTH OF EMPLOYMENT - ABOUT 3PCT - TO COPE WITH NEW ENTRANTS TO THE JOB MARKET AND RETURNING GUEST-WORKERS. AS A RESULT OF THE ENERGY CRISIS AND SUBSEQUENT ECONOMIC DEVELOPMENTS, YUGOSLAVIA CAN NO LONGER COUNT ON A NET EXPORT OF LABOUR TO WESTERN EUROPE TO REDUCE ITS OWN SURPLUS POSITION. WITH THE NUMBER OF EMPLOYED AT ABOUT 4.5 MILLION, UP TO AN AVERAGE 10PCT OF THIS NUMBER, WITH REGIONAL VARIATIONS, ARE SEEKING JOBS. A LARGE PROPORTION OF THIS FIGURE IS THE RESULT OF WORKERS LEAVING THE COUNTRYSIDE TO SEEK EMPLOYMENT IN THE CITIES. ABOUT 1/2 THE JOB SEEKERS ARE WOMEN.

10. ANY LARGE-SCALE RETURN OF YUGOSLAV GUESTWORKERS AS A RESULT OF AN ECONOMIC SLOWDOWN IN WESTERN EUROPE WOULD, IN ADDITION TO COMPOUNDING THE BALANCE OF PAYMENTS PROBLEM (SINCE THESE WORKERS ARE A PRINCIPAL SOURCE OF YUGOSLAVIA'S FOREIGN EXCHANGE EARNINGS), CREATE A CRITICAL EMPLOYMENT SITUATION WITH UNPREDICTABLE POLITICAL

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AND SOCIAL CONSEQUENCES IN YUGOSLAVIA. A YUGOSLAV TRADE UNION REPRESENTATIVE WORKING WITH THE UNION FEDERATION IN THE FRG HAS RECENTLY REPORTED A FIGURE OF 19,000 YUGOSLAVS UNEMPLOYED IN THE FRG BASED ON AN OVERALL JOBLESS TOTAL OF 800,000 (115,000 FOREIGNERS). IN ADDITION, AN ESTIMATED 10,000 TO 30,000 ILLEGALLY EMPLOYED YUGOSLAVS MAY NOW BE WITHOUT WORK. LOOKING TO THE FUTURE, THIS SOURCE PREDICTS A PEAK OFFICIAL UNEMPLOYMENT FIGURE OF 50,000. HOWEVER, SINCE THE BULK OF THESE WOULD BE ENTITLED TO UNEMPLOYMENT BENEFITS IN THE FRG, THE SOURCE ANTICIPATES ONLY A SMALL SCALE RETURN TO YUGOSLAVIA, ALTHOUGH THIS ASSESSMENT DOES

NOT APPEAR TO TAKE ACCOUNT OF THE SITUATION OF THE "ILLEGALS" WHO WOULD BE WITHOUT BENEFITS. A RETURN OF GUESTWORKERS TO YUGOSLAVIA LIMITED TO THE SCALE SUGGESTED BY THESE FIGURES WOULD PRESENT A PROBLEM BUT ONE WHICH WOULD PROBABLY NOT BECOME CRITICAL. THE SITUATION HOWEVER IS CLEARLY UNCERTAIN AND FLUID AND COULD DETERIORATE FAIRLY RAPIDLY.

11. ON THE WHOLE, GIVEN THE CURRENT INTERNATIONAL SITUATION, FOR YUGOSLAVIA TO MEET THE FOREIGN TRADE TARGETS SET IN THE RESOLUTION ON ECONOMIC AND SOCIAL POLICY FOR 1975 WILL REQUIRE A VERY DETERMINED EFFORT AND PROBABLY A VERY HEFTY DOSE OF GOOD FORTUNE. MUCH WILL DEPEND ON THE INTERNATIONAL ECONOMIC SITUATION, PARTICULARLY THAT IN WESTERN EUROPE, BOTH BECAUSE OF THE YUGOSLAV GUESTWORKERS THERE AND ALSO ITS IMPORTANCE AS A YUGOSLAV MARKET. UNDER CURRENT CIRCUMSTANCES, IT IS DIFFICULT TO SEE MUCH SLACKENING IN THE PRESENT RATE OF INFLATION HERE, WHICH IN TURN WILL MAKE THE PLANNED INCREASE IN EXPORTS, WHICH IS FUNDAMENTAL IN THE RESOLUTION, MORE DIFFICULT TO ATTAIN IN A VERY COMPETITIVE INTERNATIONAL MARKET. NOR, GIVEN RECENT EXPERIENCE, DOES THE VERY LIMITED TARGET FOR THE REAL GROWTH IN IMPORTS APPEAR VERY REALISTIC IN THE ABSENCE OF MORE VIGOROUS MEASURES TO ACHIEVE THIS GOAL. YUGOSLAVIA, THEREFORE MAY WELL BE HARD-PRESSED TO OVERCOME ITS BALANCE OF PAYMENTS DEFICIT DESPITE LAST FALL'S 7PCT DINAR DEVALUATION. IF THIS IS NOT DONE HOWEVER, THE DEFICIT WILL NEED TO BE FINANCED BY FURTHER INTERNATIONAL BORROWING ENTAILING HIGHER FUTURE REPAYMENT OBLIGATIONS. THIS, IN TURN, WOULD MEAN THAT THESE RESOURCES WERE NOT AVAILABLE FOR PRODUCTIVE INVESTMENTS TO AID IN OVERCOMING LONG-TERM DEVELOPMENTAL REQUIREMENTS. THUS, THE YUGOSLAV ECONOMY, FACES SOME VERY DIFFICULT SHORT-RUN, AS WELL AS CONTINUING, PROBLEMS. TO MEET THESE, THE LEADERSHIP ARE MAKING STEADY EFFORTS TO MOBILIZE ALL OF YUGOSLAVIA
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THROUGH THE VARIOUS LEADING SOCIO-POLITICAL ORGANIZATIONS (THE LCY, THE TRADE UNIONS, THE SOCIALIST ALLIANCE) TO SUMMON FORTH NATIONAL WILL THAT IS REQUIRED. STATEMENTS BY THE LEADERSHIP REPEATEDLY STRESS THE NECESSITY OF HARMONIZING ECONOMIC ORGANIZATION WITH THE SELF-MANAGEMENT SYSTEM OF THE NEW 1974 CONSTITUTION. EFFECTIVE SELF-MANAGEMENT BY THE WORKERS IS APPARENTLY SEEN AS A FORMULA FOR PROMOTING RATIONALIZATION AND EFFICIENCY IN THEIR OWN SELF-INTEREST WHICH WOULD EASE YUGOSLAVIA'S ECONOMIC PROBLEMS. SELF-MANAGEMENT ON THE CURRENT SCALE HOWEVER INVOLVES AN ECONOMIC SYSTEM WHERE DECISION-MAKING HAS BECOME VERY COMPLEX AND DIFFUSE, HENCE THIS MOBILIZATION EFFORT MUST RELY FOR SUCCESS PRIMARILY ON MORAL SUASION AND NEGOTIATED "SELF-MANAGEMENT AGREEMENTS" ECOMPASSING UNDERTAKINGS TO ACHIEVE FAVOURABLE ECONOMIC OBJECTIVES. WHETHER THIS WILL PROVE SUFFICIENT OR WHETHER OTHER MEASURES (SUCH AS PERHAPS A FURTHER DINAR DEVALUATION) WILL EVENTUALLY BE NEEDED WILL HAVE TO AWAIT DEVELOPMENTS IN THE NEXT FEW MONTHS. END TEXT. BRUCE

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